Contemporary Issues in Consumer Bankruptcy
Introduction

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The financial crisis hit households and individuals hard, yet the political discourse has focused nearly exclusively on the banking system and the debt crises of certain European nations. When policymakers focus on consumer debtors, the debate is mostly limited to a discussion of individual responsibility. But as the current situation in many European countries shows, over-indebtedness is closely related to macroeconomic changes at global and national levels.

During the last twenty years, many countries have taken up legal measures to alleviate the situation faced by over-indebted individuals and households. Especially in Europe, debt adjustment laws that resemble Anglo-Saxon consumer insolvency procedures leading to partial or total discharge of excessive debt have been adopted. In this book, legal developments and experiences in the Netherlands, Sweden, Austria, and Germany are reported. In the Netherlands, debt adjustment is connected with the idea of prevention and consumer protection. Traditionally, debts have been renegotiated successfully. Nadja Jungmann and Nick Huls analyze the problems related to this renegotiation approach in a new environment of credit and court imposed discharge. The Swedish attitude toward the discharge of debt instead has been quite restrictive. Annina H. Persson takes up the recent reform of this debt adjustment law, in which the institutional setting has been changed to open access to the procedure. In Austria, emphasis has been on individual debtors’ repayment schemes, a bankruptcy process that has been in force for a decade now. Georg E. Kodek provides empirical evidence to suggest that the procedure has been a success.

Besides debt adjustment procedures, consumer protection measures have a role in the prevention and alleviation of consumer over-indebtedness. In Europe, the new consumer credit directive (2008) does not address over-indebtedness, nor do any other European Union instruments. Johanna Niemi sees over-indebtedness as a problem that should be addressed with the integration of the markets. She takes up the Council of Europe Recommendation as an example of how a common policy might be pursued. Michelle Kelly-Louw discusses problems encountered with raising interest levels in South Africa. Interest rate increases pose serious problems to individual debtors and households, especially at times of economic insecurity. Souichirou Kozuka analyzes how consumer protection law, both judge-made law and legislation, has developed and interacted in Japan to approach consumer over-indebtedness.
Stephanie Ben-Ishai and Saul Swartz take up the role of the public sector creditors in the processes of indebtedness. In welfare societies, the government and public sector are important sources of economic support, both to households and businesses. Government subsidies are in some cases paid on conditions that remain unfulfilled and the subsidy will be collected back. The public also plays a role as a creditor in its function of tax collector. The role of public creditors has largely been unacknowledged in research on over-indebtedness so far.

We also need more empirical and qualitative research on over-indebtedness as a social problem. Several studies report on different factors leading to over-indebtedness. In this book, research by Michael Knoblauch and by Eva Münster et al. from Germany as well as by Cláudia Abreu Lopes, Catarina Frade and Fernanada Jesus from Portugal report that loss of employment, small business failure, health problems, changes in family relations, and inadequate handling of financial affairs are common factors in the cases of over-indebtedness. These factors are often seen as factors leading to over-indebtedness and insolvency but recent studies, such as that by Eva Münster et al., indicate that over-indebtedness is also a cause of or at least a factor contributing to, for example, health problems. When this causal link is acknowledged, the enormous cost of over-indebtedness to societies becomes more visible.

The contributions in this book are based on presentations at the conference Over-indebtedness: Everyday Risk in Modern Societies? Theoretical Aspects and Empirical Findings in International Perspective, organized by the Department of Sociology at Chemnitz University of Technology, between March 26 and 28, 2009. The conference gathered together an international network of scholars conducting socio-legal and comparative research in issues of consumer over-indebtedness and insolvency.

We thank Fritz Thyssen Stiftung for financing this conference. We also thank Alice Neffe, of the Helsinki University, and the many students at Chemnitz Technical University who assisted the editors with the technical part of editing this book.

Two chapters are based on earlier published work. We thank the US-China Law Review and the Queen’s Law Journal for the permissions to reprint the articles.

Berlin, Helsinki and New York

Wolfram Backert, Susan Block-Lieb and Johanna Niemi
Never too Small to Fail: Insolvency of Consumers as an International Concern
Johanna Niemi

Introduction

*Individual debtors in the rescue discourse*

We live in the midst of the worst economic crisis since the 1930s. The crisis that started in 2007 and was first characterized as the bursting of the housing bubble in the United States has now spread all over the world. In late 2008, after the collapse of the investment bank Lehman Bros., the crisis discourse was framed as a debate over the default or the rescue of banks and the banking system. The possibility of certain large banks’ failure was seen as a threat to the whole financial system – hence the notion that some banks were too large to fail.² Fears of the collapse of the financial sector have been prevailing since. A third turn in the framing of the crisis discourse took place in 2010 in Europe when first Greece and then Ireland were unable to meet its credit obligations. Portugal and Spain now have also received bailout funds. The problems of national economies, particularly those in the Euro zone, have started to denominate the discussion and the framing of the crisis.

Individual debtors have been strangely absent from the public discourse, although they were first pointed out as the precursor of the crisis with the housing bubble. That the financial crisis hit individual debtors is a generally known fact, but it may take a long time before the full effect of the economic crisis on ordinary households is revealed. Articles in this book, as well as previous research, demonstrate the mounting distress and suffering of over-indebted consumers.³ In this book, Eva Münster et al. show how health problems are strongly correlated to individuals’ debt problems, both as a cause and a consequence. Claudia

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1 I thank Wolfram Backert and his colleagues at Chemnitz University of Technology for organizing the conference, at which this paper was first presented, and also the participants of that conference for comments and exchange of ideas. I also thank Susan Block-Lieb for valuable editing of this chapter.
2 Stiglitz 2010.
3 See, for example, Sullivan et al. 1989 and 2000; Niemi-Kiesiläinen et al. (eds) 2003 and 2009; Towards a common operational European definition 2008. In this chapter, the term consumer debtor refers in the context of insolvency law to any debtor who is seeking relief in his or her private capacity. The debts are not necessarily incurred by consumption. There may be housing debts, tax debt and debts from an already closed business etc. In the context of insolvency law, the term consumer is used in this broad meaning.
Lopes, Catarina Frade and Fernanda Jesus describe the problems that overindebted Portuguese debtors have suffered in a time of growing unemployment before the debt situation of Portugal became front page news in the spring 2011. Michael Knoblauch and Götz Lechener analyze in their respective articles the situation that German debtors face, both when they come and seek help from debt advisors and when they file for consumer insolvency in the courts.

The possibility that troubled banks’ insolvencies would drag down entire economies led to demand for bank bailouts. Ordinary debtors’ insolvencies have not evoked equally strong demands for rescue as have banks’ troubles. Ordinary debtors have never been too small to fail.

As Joseph Stiglitz has argued, the current crisis may be a symptom of deeper changes in the economic and political system. Deregulation of the financial system has led to an increasing instability of the global economic order since the Second World War. As a consequence, different parts of the world have experienced successive economic crises: Latin America in the beginning of the 1980s; many parts of Europe in the late 1980s and early 1990s; East Asia 1997-98 and Europe and the United States in the early 2000s (Internet bubble); and now this nearly global crisis, which began in 2007 or 2008. All these preceding crises can be attributed, at least in part, to the deregulation of the credit markets and overheating of investments in specific assets in certain parts of the world. Therefore, it was natural to interpret the current crisis as a symptom of inflated housing prices and an unregulated market in sub-prime mortgages and residential mortgage backed securities.

For ordinary people, deregulation of the financial services industries has meant the democratization of consumer credit by making credit available to a wider breadth of people than before. But increased access to credit has also made a wider swath of people vulnerable to default when the economy hit a downturn. Indeed, each of the mentioned economic crises has brought with it an increase in the number and distribution of households with serious debt problems. As the articles in this book show, many States that have been hit by an economic crisis have taken steps to solve the problem of over-indebtedness. There seems to be a fundamental difference in the approaches that governments apply when seeking to resolve the financial difficulties faced by banks, nation-states and ordinary people.

Political discourse on the crisis of the banking system focused on rescue. Banks’ threatened illiquidity invoked strong demands for rescue operations by national governments. In many countries, governments infused capital into the

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4 Such analysis is presented also by Ferguson 2008 and Rajan 2010.
banking system in order to sustain the overall functioning of the financial sector. In the United States, TARP (Troubled Asset Relief Program) funding was made available to nearly all banks, no questions asked. Even before Congress authorized TARP funding, the US Federal Reserve System bolstered the liquidity in this sector by lending on the most favourably terms through its discount window. The Bank of England similarly provided liquidity support for failing financial entities, such as Northern Rock. In Europe, Member States of the European Union and the European Central Bank have combined their efforts to adopt a variety of liquidity measures. There have been differing solutions. The European Union has issued bonds to consolidate Member States’ loans; the governments of some Member States unilaterally have strengthened the share capital of some banks; in others, the government bought bad loans. Rescue operations are always urgent; in the heat of the moment the conditions for loans and capital cannot be deliberated upon in great detail.

We have not seen equally urgent rescue packages for individual debtors. The problem of individuals’ over-indebtedness is examined solely in the national context. National legislatures have, indeed, taken steps to help over-indebted consumer debtors and households, but usually only after the urgency of the crisis is over. This book, as well as prior comparative research on consumer insolvency, shows that the measures taken to enable consumers access to an insolvency regime, or to reform the terms on which such access is granted, vary a great deal, depending on the economic system, legal traditions and culture, and the depth of the crisis. Chapters in this book give several examples of national legislatures’ responses to the problems of the over-indebted debtors. Chapters by Michelle Kelly-Louw and Souichirou Kozuka contain several examples of the ways in which consumer protection and consumer credit laws have been amended in South Africa and Japan to prevent or otherwise address debt problems and the potential for unintended consequences as these laws are implemented.  

*Rescue through personal insolvency*

In many cases, rescue has taken the form of consumer debt adjustment laws. Consumer debt adjustment law or, in the American legal usage consumer bankruptcy law, means, in this context, a judicially supervised procedure, in which the debtor can receive relief from part of her debts through confirmation of a payment plan that obliges the debtor to pay the remaining portion of her debt.

Before the 1990s, this legal institution was seen in other parts of the world as an Anglo-Saxon curiosity. The insolvency laws in other parts of the world

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5 Kelly-Louw et al. 2008. See also discussion and examples in Niemi-Kiesiläinen et al. 2009.